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No. 98-1101

In the
Supreme Court Of The United States

October Term, 1998

ROHN F. DRYE, JR., SUE C. DRYE, THERESA K. DRYE AND THE DRYE FAMILY 1995 TRUST, DANIEL M. TRAYLOR, TRUSTEE,

Petitioners,

vs.

UNITED STATES OF AMERICA,

Respondent.

On Writ of Certiorari
To the United States Court of Appeals
For The Eighth Circuit

BRIEF FOR THE PETITIONERS

Daniel M. Traylor
Counsel of Record
Law Office of Daniel M. Traylor
900 West Third Street
Little Rock, AR 72201
(501) 372-3330

Attorney for the Petitioners

CornerStone Graphic, Inc., Little Rock, AR

2589

QUESTION PRESENTED

Whether the interest of an heir in an estate constitutes "property" or a "right to property" to which the federal tax lien attaches under 26 U.S.C. 6321 even though the heir thereafter purports retroactively to disclaim the interest under state law.

or

When, if at all, does the federal tax lien under 26 U.S.C. 6321 attach to a lineal descendant's rights in an intestate's estate.

PARTIES TO THE PROCEEDING

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A. The taxpayer's interest in the intestate's estate under state law consisted of a personal right of decision to accept or reject the gift of inheritance, and as such does not constitute "property" or "rights to property" under state law.

B. The taxpayer's interest in the intestate's estate under federal law cannot be "property" or "rights to property" because such interest was without pecuniary value and was non-transferable.

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BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App.1a - 18a) is reported at 152 F.3d 892. The orders and judgment of the U.S. District Court, Eastern District of Arkansas, Western Division, are unreported, but are reproduced at Pet. App. 19a - 29a.

JURISDICTION

The judgment of the court of appeals was entered on August 17, 1998. A petition for certiorari was filed on November 16, 1998 and granted on April 19, 1999. The Court's jurisdiction is based on 28 U.S.C. §1254(1)(1994).

LEGAL PROVISIONS INVOLVED IN THIS CASE

Internal Revenue Code (26 U.S.C.):
§6321
§7426(a)(1)

Arkansas Code Ann. (Michie 1987):

Ark. Code Ann. §28-1-102(a)(10)
Ark. Code Ann. §28-1-104(a)(1)(5)(7)

These provisions are set forth at the Appendix hereto.

Internal Revenue Code (26 U.S.C.):
§6331(a)

Arkansas Code Ann. (Michie 1987):

Ark. Code Ann. §28-2-101
Ark. Code Ann. §28-2-102
Ark. Code Ann. §28-2-108
Ark. Code Ann. §28-9-203

These provisions are set forth at Pet. App. 30a - 33a.

STATEMENT

In November 1989, an engineering firm owned by Petitioner Rohn F. Drye, Jr., then age 66, failed through an involuntary liquidation, leaving Mr. Drye insolvent. One of his many creditors was the Internal Revenue Service. In 1990 and 1991, the Service assessed income and other taxes and various penalties against Mr. Drye. Because Mr. Drye was unable to pay these assessments, the Service filed notices of tax lien upon "all

property and rights to property" belonging to him (26 U.S.C. §6321) App 1 .

On August 3, 1994, Mr. Drye's mother, widow Irma Delilah Drye, age 89, died intestate at her home in Pulaski County, Arkansas. Her estate was valued at approximately $233,000, of which $158,000 was personalty and $75,000 was the homestead. She was survived by two lineal descendants, her son Rohn and his daughter, Petitioner Theresa K. Drye, then age __. At the time of his mother's death, Mr. Drye was insolvent and owed the Service approximately $325,000 on the unpaid tax assessments for which notices of tax lien had been filed.

Mr. Drye was appointed administrator of his mother's estate by the Pulaski County, Arkansas Probate Court on August 17, 1994. On February 6, 1995, Mr. Drye filed in instrument entitled "Disclaimer and Consent" with the probate court in which he rejected the gift of inheritance of his mother's estate. On February 7, 1995, the probate court accepted Mr. Drye's resignation as administrator and appointed Theresa as successor administratrix. On March 10, 1995, the probate court entered an order authorizing the final distribution of estate assets to Theresa as the sole heir of her grandmother's estate under state law.

Later, Theresa funded the Petitioner, Drye Family 1995 Trust, with the assets she received as her property under the probate court order of final distribution. The beneficiaries of the trust are Theresa, and during their lifetime, Mr. Drye and his wife, Petitioner Sue C. Drye. Distributions are discretionary with the trustee and may be made only for the health, maintenance and support of the beneficiaries. The trust is spendthrift.

In April, 1995, Mr. Drye approached the Service in an effort to compromise and settle his tax liabilities. During negotiations, he disclosed his beneficial interest in the trust. On

April 11, 1996, the Service levied upon an account held in the trust's name at an investment company and seized $134,004.33. On the same day, the Service filed a notice of tax lien against the trust, as Mr. Drye's nominee, encumbering the trust's real property (i.e. the former family homestead) and all its personal property.

On May 1, 1996, the trust filed a wrongful levy action against the United States in the U.S. District Court, Eastern District of Arkansas under 26 U.S.C. §7426 (a) (1). App. 1 . The trust contended that Mr. Drye never had any recognized or enforceable right, at law or in equity, in the trust property encumbered, levied and seized by the Service.

The Government answered with a general denial and counterclaimed to foreclose the trust's equity of redemption in the former homestead and to reduce to judgment the assessments against Mr. Drye.

Th[illegible] and the Government both moved for summary judgment. The district court granted the Government's motion. Pet. App. 19a. The court concluded that Mr. Drye "obtained a vested interest in the estate property of his mother upon her death to which the federal tax liens attached so that the state disclaimer law that was later invoked was incapable of removing those federal liens." *Id.* at 23a.

In response to the trust's motion for reconsideration, the court conceded "that Arkansas law is used to determine the legal interest Rohn had in the property against which the tax lien is attached, but federal law governs when the tax liens attached." *Id.* at 26a. The court then stated "a state disclaimer law that is later invoked after the liens properly attached cannot remove those federal liens." *Id.* at 26a.

The court of appeals affirmed. Pet. App. 1a - 18a. The court explained that, under the federal tax lien statute, the court is to look to state law to determine "whether a given set of circumstances creates a right or interest" (*id.* at 12a) and then look to federal law to determine whether that right or interest constitutes "property" or "rights to property" under 26 U.S.C. §6321 to which the federal tax lien attaches. Pet. App. 12a - 13a (citing *United States v. National Bank of Commerce*, 472 U.S. 713, 727 (1985)). See also *id.* at 6a - 8a. The court held that an interest in property under state law constitutes "property" or "rights to property" under federal law (to which the federal tax lien attaches under 26 U.S.C. §6321) if the interest is transferable and has pecuniary value (Pet. App. 7a, 14a).

The court of appeals concluded that Mr. Drye's right to inherit the property of his mother's estate satisfied this standard because that right was transferable and had pecuniary value (Pet. App. 8a, 14a). Mr. Drye's interest thus represented "property" or "rights to property" for purposes of the federal tax lien statute, and the tax liens filed against Mr. Drye attached to his right to inherit his mother's estate. *Id.* at 13a.

The court explained that Mr. Drye's subsequent disclaimer of his interest under state law could not, by legal fiction, extinguish the federal liens that previously attached to that interest. The fact that the disclaimer is treated as if it relates back to the date of the decedent's death does not mean that, at the time the lien attached, Mr. Drye held no "property" or "rights to property" in the estate. Because the federal liens validly attached to that property before the disclaimer was made, Mr. Drye's subsequent renouncement could not defeat the federal lien. Title to the property transferred to the trust remained subject to the preexisting federal tax lien, and the levy on the assets of the trust to satisfy Mr. Drye's debt was therefore not wrongful. Pet. App. 4a - 5a, 17a - 18a.

SUMMARY OF ARGUMENT

I.A. In or about 1991, the IRS made assessments against taxpayer Rohn F. Drye, Jr. and, under I.R.C. §6321 federal liens attached to all of his property and rights to property. In 1994, Mr. Drye's mother died intestate in Pulaski County, Arkansas leaving two lineal descendants, Mr. Drye and his daughter, Theresa K. Drye. In 1995, the probate court with jurisdiction to determine heirship adjudged that Theresa was the sole heir of her grandmother's estate because Mr. Drye had legally exercised his personal right of decision to reject the inheritance under state law. As a consequence, the probate court ordered the distribution of the estate's assets to Theresa. Theresa, in turn funded a family trust with the assets distributed under the authority of the probate court. When Mr. Drye explained these events to the IRS, the Service seized $134,000 of the trust's funds and moved to foreclose an alleged tax lien against the trust's real estate.

The trust then brought an action against the Government to recover the funds seized and to enjoin the Government's foreclosure procedure. The federal courts below upheld the Government's seizure on the theory that the federal lien of I.R.C. §6321 attached at the instant of her death to Mr. Drye right to succeed to his mother's estate and that his subsequent disclaimer under state law could not extinguish the federal lien once attached.

The federal courts below erred in their analysis because under federal law, Mr. Drye never acquired property or rights to property in his mother's estate as required under I.R.C. § 6321.

Under state law, at the instant of her death, Mr. Drye acquired a mere right of personal decision to accept or reject the gift of inheritance of his mother's estate. Mr. Drye lawfully elected to reject the gift. This personal right of decision to accept

or reject the gift of inheritance under state law was not property or rights to property under federal law, because the right was personal to Mr. Drye, could not be the subject of a transfer or assignment, and could not be bargained away or exchanged for anything of pecuniary value. Because Mr. Drye disclaimed, his birthright to otherwise succeed to his mother's estate remained unvested, inchoate, unrecognized, and unenforceable, at law or in equity, under state law. Consequently, there was no property or rights to property to which the federal lien could attach.

ARGUMENT

I. THE FEDERAL COURTS BELOW ERRED IN HOLDING THAT THE FEDERAL TAX LIEN OF I.R.C. §6321 ATTACHED TO THE TAXPAYER'S INTEREST IN THE INTESTATE'S ESTATE BECAUSE THAT INTEREST DOES NOT CONSTITUTE "PROPERTY" OR "RIGHT TO PROPERTY" AS REQUIRED UNDER FEDERAL LAW.

A. The taxpayer's interest in the intestate's estate under state law consisted of a personal right of decision to accept or reject the gift of inheritance, and as such does not constitute "property" or "rights to property" under state law.

The issue is whether the federal courts below correctly interpreted federal and state law in holding that a federal tax lien attached to Mr. Drye's "rights" in his mother's estate upon her last breath so as to justify the seizure and encumbrance of the estate's assets. The answer is no.

When a person fails to pay his taxes, after assessment, all property rights that he has or acquires thereafter immediately and automatically are subject to a federal tax lien, see 26 U.S.C. §6321 and *United States v. Security Trust & Sav. Bank*, 340 U.S. 47, 51, 71 (1950). Section 6321 does not, however, create or define what constitutes a property interest. Instead, state law determines whether a taxpayer has a property interest to which a federal lien may attach. See *United States v. National Bank of Commerce*, 472 U.S. 713, 722-23, *Aquilino v. United States,* 363 U.S. 509, 513 (1960); *United States v. Bess,* 357 U.S. 51, 55 (1958). Therefore, the Court must decide whether under

applicable state law, Mr. Drye ever had a property interest in his mother's estate.

At common law in both England and the United States, it was settled that a taker of property under a will had the absolute right to accept or reject a legacy or devise. See *Unif. Disclaimer of Transfer by Will, Intestacy or Appointment Act*, 8A U.L.A. 166, 166-68 (1993). It was said that no one can make another an owner of an estate against his consent. The legacy or devise was deemed a gift, and thus a bilateral transaction, requiring not only a donor's intent to give, but also a donee's acceptance. Under the rule, the disclaimed interest related back to the date of the testator's death so that the interest did not vest in the grantee, but remained in the original owner as if the will had never been executed. Devolution of the interest was generally treated the same as in case of lapse.

However, an "heir" had no common law power to prevent passage of title to himself by disclaimer. "An heir at law is the only person whom the law of England vests property, whether he will or not. No disclaimer that he may make will have any effect, though, of course, he may as soon as he pleases dispose of the property by ordinary conveyance." Williams on Law of Real Property, 75 (2d. Am. Ed. 1857).

The difference between testate and intestate successions in respect to the right to disclaim produced a number of illogical and undesirable consequences. See *Jake Looney, Use of the Disclaimer as an Estate Planning Device under Arkansas Law*, Ark. L. Notes 67 (1985). For example, an heir who sought to reject his inheritance was subjected to the Federal gift tax on the theory that since he could not prevent the passage of title to himself, any act done to rid himself of the interest necessarily involved a transfer subject to gift tax liability. *Hardenberg v. Com'r*, 198 F. 2d. 63 (8th Cir.), *cert. denied*, 344 U.S. 863 (1952).

Conversely, a legatee or devisee who rejected a legacy or devise under a will incurred no such tax consequences. *Brown v. Routzahn*, 63 F. 2d. 914 (6th Cir.), *cert. denied*, 290 U.S. 641 (1933). Moreover, the difference between testate and intestate successions, rooted in the feudal theory that a contrary rule would allow an heir to break or bar an estate in tail, became something of an anachronism.

Arkansas law concerning the vesting of estates and the right of renunciation was clarified with the State's adoption of General Act 457 of 1973 as codified at Ark. Stat. Ann. §§62-3201-3210 (Bobbs-Merrill Cum. Supp. 1973, repealed 1981). Section 16 of Act 457 is on point:

> SECTION 16. Emergency clause. It is hereby found and determined by the General Assembly of the State of Arkansas that a disclaimer has not been heretofore defined by this legislative body, that confusion and uncertainty surround the manner in which beneficiaries and heirs should decline testamentary gifts and intestate inheritances, as well as the subsequent disposition to be made of any gift or inheritance so declined, and that the immediate passage of this Act is necessary to provide legislative guidance in this area. Ark. Code Ann. §62-3210 (Bobbs-Merrill Cum. Supp. 1973).

Significantly, Mr. Drye's disclaimer would have been void under Act 457 because of Section 8 thereof which provided:

> SECTION 8. Insolvency. The right to disclaim otherwise conferred by the provisions of this Act shall be barred if the beneficiary is insolvent at the time of the event giving rise to the right to disclaim. Ark. Stat. Ann. §62-3208 (Bobbs-Merrill Cum. Supp. 1973, repealed 1981).

See *Elliott v. Hardcastle*, 271 Ark. 90 (1980); *Legislative Survey, Decedent's Estates*, 4 UALR L.J. 591.

The relevant law is now General Act 348 of 1981 and codified in the Arkansas Probate Code as Ark. Code Ann. §§28-2-101 - 109. Act 348 expressly repeals Act 457 of 1973 and Section 8 thereunder. Such Act now provides in pertinent part:

> Section 1. Rights to disclaim interest in property. A person to whom any property or interest therein devolves, by whatever means, may disclaim it...by delivering a written disclaimer under this chapter. Ark. Code Ann. §28-2-101 (Michie 1987).

> Section 2. Waiver and bar. The right to disclaim property or an interest therein is barred by: (1) An assignment, conveyance, encumbrance, or a contract therefor; (2) A written waiver of the right to disclaim; (3) An acceptance of the property or interest or a benefit thereunder; (4) A sale of the property or interest under judicial sale made before the disclaimer is affected. Ark. Code Ann. §28-2-102 (Michie 1987).

> Section 7. Time of disclaimer - Delivery. (a)(1)... If the property or interest has devolved to the disclaimant by the laws of intestacy, the disclaimer shall be delivered...not later than nine (9) months after the death of the deceased owner. Ark. Code Ann. §28-2-107.

Mr. Drye's Disclaimer and Consent is in good statutory form because it satisfies each and every requirement of Act 348. The legal effect of Mr. Drye's Disclaimer and Consent is provided by:

> Section 8. Effect of disclaimer. (a)(1) If the property or interest devolved to a disclaimant under the law of intestacy...it devolves as if the disclaimant had predeceased the decedent. (3) A disclaimer relates back for all purposes to the date of death of the decedent. (emphasis added) Ark. Code Ann. §28-2-108 (Michie 1987).

Neither the Arkansas Supreme Court nor the Arkansas Court of Appeals has had occasion to interpret Act 348. Nevertheless, the Court must do its duty as pronounced in *Fidelity Union Trust Co. v. Field*, 311 U.S. 169, 177 (1940):

> ... The highest state court is the final authority on state law ... but it is still the duty of the federal courts, where the state law supplies the rule of decision, to ascertain and apply that law even though it has not been expounded by the highest court of the State.

Petitioner notes that Act 348 mirrors the Uniform Disclaimer of Property Interest Act of 1978 promulgated by the Section on Real Property, Probate and Trust Law of the American Bar Association. The official commentaries of the uniform act have been made part of the Arkansas Code of 1987 as published at page 502 of the Commentaries volume which provides:

> "As regards creditors, taxing authorities and others, the provision for "relation back" has the legal effect of preventing a succession from becoming operative in favor of the disclaimant.

> The relation back is "for all purposes: which would include, among others, for the purpose of rights of creditors and taxing authorities." Similarly, numerous cases have held that a devisee or legatee can disclaim a devise or legacy despite the claims of creditors; *Hoecker v. United Bank of Boulder*, 476 F.2d 838 (C.A. 10, 1973) aff'g 334 F.Supp. 1080 (D.Colo. 1971) (bankruptcy); *United States v. McCrackin*, 189 F. Supp. 632 (S.D. Ohio 1960) (Federal income tax liens).

The only reported case to construe Act 348 issued from the district court below. See *Hurt v. United States*, 566 F. Supp. 356 (E.D. Ark., 1983). There the district court found that the relation back doctrine had the legal effect of passing the estate in question directly (emphasis added) to the non-disclaiming lineal descendants of the intestate decedent. This case supports inferentially that Mr. Drye acquired no property interest in the decedent's estate. *Id.* at 358.

At the moment of his mother's death, Mr. Drye acquired nothing more than a personal right of decision as to whether to accept or reject the gift of inheritance offered. This personal right of decision did not constitute property or rights to property under 26 U.S.C. §6321 because the right had no pecuniary value and was not transferable. By definition, a descendent cannot receive any consideration for execution and delivery of a disclaimer, and the right to disclaim is personal to the descendent and cannot be assigned or otherwise transferred to others without invoking the bar of Ark. Code Ann. §28-2-102.

B. The taxpayer's interest in the intestate's estate under federal law cannot be "property" or "rights to property" because such interest was without pecuniary value and was non-transferable.

The federal courts below went astray from the proper application of federal when they assumed that the legal fiction lurking in this case is the relation back of Mr. Drye's disclaimer. Pet. App. 8a, 13a, 14a, 17a. In *United States v. Irvine*, 511 U.S. 224 (1994) the court recognized that the right to disclaim might, under state law, be based on a gift acceptance-rejection theory and be, therefore not a legal fiction, but reality. *Id.* at 239-40. The court of appeals incorrectly found that reality is located at Ark. Code Ann. §28-9-203(c). This statute provides that real estate passes immediately to the heirs upon the death of an intestate, subject to probate administration, and that personalty passes to the administrator for distribution to the heirs unless otherwise disposed of as permitted by the Arkansas Probate Code. The federal courts below got it backwards. The legal fiction is Section 28-9-203(c). Upon the death of an intestate, the property passes to his or her estate for administration.

Petitioners assert that under the Arkansas Probate Code, Mr. Drye never was an "heir" of his mother's estate. This assertion is based upon the jurisdiction of the probate courts to determine in the first instance the heirs of an intestate decedent. Ark. Code Ann. §28-1-104(a)(5) ("the probate court shall have jurisdiction over...the determination of heirship"). Here the probate court adjudged that only Theresa K. Drye met the legal definition of an heir under the Arkansas Probate Code; Mr. Drye's status never exceeded that as a lineal descendant of the intestate decedent. This finding is consistent with the gift acceptance-rejection theory of the succession of estates under state law.

Another error by the federal courts below is their finding that under state law, the right to inherit has pecuniary value and is transferable. Pet. App. 9a. In the first instance, Petitioners assert that all of the cited cases appear to be determined under prior law, but more importantly, all of the cases beg and bootstrap the fundamental issue involved here, i.e., when, if at all, does a lineal descendant acquire a valuable right in an intestate's estate under the Arkansas gift acceptance-rejection theory of succession of estates. The answer is found in statutory analysis. The succession vests, if at all, at the moment the descendant acts so as to bar the exercise of his personal right of decision to disclaim under Ark. Code Ann. §28-2-102, or the expiration of nine months from the date of the intestate's death, whichever is earlier. In all the cases cited by the court of appeals, the parties involved were already vested with the property, estate or other interest involved and thus were precluded from the exercise of the personal right of decision to disclaim.

The circuit panel below was misguided in parting company with the Fifth and Ninth Circuits of Appeal in near identical factual and legal cases and instead purported to side with the Second Circuit. See *Leggett v. United States*, 120 F. 3d. 592 (5th Cir., 1997), *Mapes v. United States*, 15 F. 3d. 138 (9th Cir., 1994) and *United States v. Comparato*, 22 F. 3d. 455 (2nd Cir., 1994), respectively. First, there is no real conflict between the decisions in these three cases. Petitioner agrees with the Government and the Eighth Circuit that Comparato was correctly decided. The critical fact in Petitioners' view is that notwithstanding the peculiarities of New York law, the disclaimer there was executed seven years after the date of death of the decedent involved.

CONCLUSION

For all the foregoing reasons, the decision of the court of appeals should be reversed.

Respectfully Submitted,

Daniel M. Traylor
Counsel of Record
Law Office of Daniel M. Traylor
900 West Third Street
Little Rock, AR 72201
(501) 372-3330

Attorney for the Petitioners

APPENDIX

26 U.S.C. §6321 Lien for Taxes

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property whether real or personal, belonging to such person.

26 U.S.C. §7426(a)(1) Civil Actions by Persons Other than Taxpayers

(a) Actions permitted.

(1) Wrongful levy. If a levy has been made on property or property has been sold pursuant to a levy, any person (other than the person against whom is assessed the tax out of which such levy arose) who claims an interest in or lien on such property and that such property was wrongfully levied upon may bring a civil action against the United States in a district court of the United States. Such action may be brought without regard to whether such property has been surrendered to or sold by the Secretary.

Ark. Code Ann. 28-1-102(a)(10) Definitions (Heir)

(a) As used in this code, unless the context otherwise requires:

(10) "Heir" denotes a person entitled by the law of descent and distribution to the real and personal property of an intestate decedent, but does not include a surviving spouse

Ark. Code Ann. 28-1-104(a) Probate Courts

(a) The probate court shall have jurisdiction over:
(1) The administration, settlement, and distribution of estates of decedents;
(2) The probate of wills;
(3) The persons and estates of minors;
(4) Persons of unsound mind and their estates;
(5) The determination of heirship or of adoption;
(6) Concurrent with the jurisdiction of other courts, the restoration of lost wills and for the construction of wills when incident to the administration of an estate; and
(7) All such other matters as are by law provided.